

Affected: IC 12-13-7-3; IC 12-15

Sec. 11. (a) Costs applicable to services, facilities, and supplies furnished to the provider by organizations related to the provider by common ownership or control may be included in the allowable cost in the unit of service of the provider at the cost to the related organization. However, such cost must not exceed the price of comparable services, facilities, or supplies that could be purchased elsewhere in an arm's-length transaction.

(b) Common ownership exists when an individual, individuals, or any legal entity possesses ownership or equity of at least five percent (5%) in the provider as well as the institution or organization serving the provider. An individual is considered to own the interest of immediate family for the determination of percentage of ownership. The following persons are considered immediate family:

- (1) Husband and wife.
- (2) Natural parent, child, and sibling.
- (3) Adopted child and adoptive parent.
- (4) Stepparent, stepchild, stepsister, and stepbrother.
- (5) Father-in-law, mother-in-law, sister-in-law, brother-in-law, son-in-law, and daughter-in-law.
- (6) Grandparent and grandchild.

(c) Control exists where an individual or an organization has the power, directly or indirectly, to influence or direct the actions or policies of an organization or institution, whether or not actually

exercised. A general partner is considered to control an entity.

(d) Transactions between related parties are not considered to have arisen through arm's-length negotiations. Costs applicable to services, facilities, and supplies furnished to a provider by related parties shall not exceed the lower of the cost to the related party, or the price of comparable services, facilities, or supplies purchased elsewhere. An exception to this subsection may be granted by the office if requested in writing by the provider before the annual rate review effective date to which the exception is to apply. The provider's request shall include a comprehensive representation that every condition in subsection (e) has been met. This representation shall include but not be limited to the percentage of business the provider transacts with related and non-related parties based upon revenue. When requested by the office, documentation to substantiate the provider's charges for services, facilities, or supplies to related and non-related parties, such as invoices, standard charge master listings, and remittances must be submitted.

(e) The office shall grant an exception when a related organization meets all of the following conditions:

(1) The supplying organization is a bona fide separate organization.

(2) A sufficient part of the supplying organization's business activity is transacted with other than the provider and organizations related to the supplier in common ownership or control, and there is an open competitive market for the type of services, facilities, or supplies furnished by the organization.

(3) The services, supplies, or facilities are those that commonly are obtained by institutions, such as the provider, from other organizations and are not a basic element of patient care ordinarily furnished directly to patients by such institutions.

(4) The charge to the provider is in line with the charge for such services, facilities, or supplies in the open market and no more than the charge made under comparable circumstances to others by

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the organization for such services, facilities, or supplies.

**405 IAC 1-14.6-12 Allowable costs; fair rental value allowance**

**Authority:** IC 12-8-6-5; IC 12-15-1-10; IC 12-15-21-2

**Affected:** IC 12-13-7-3; IC 12-15

**Sec. 12. Providers shall be reimbursed for the use of allowable patient-related facilities and equipment, regardless of whether they are owned or leased, by means of a fair rental value allowance. The fair rental value allowance shall be in lieu of the costs of all depreciation, interest, lease, rent, or other consideration paid for the use of property. This includes all central office facilities and equipment whose patient care-related depreciation, interest, or lease expense is appropriately allocated to the facility.**

**(1) The fair rental value allowance is calculated by determining, on a per bed basis, the historical cost of allowable patient-related property for facilities that are not acquired through an operating lease arrangement, including:**

**(A) land, building, improvements, vehicles and equipment; and**

**(B) costs;**

**required to be capitalized in accordance with generally accepted accounting principles.**

**Land, buildings, and improvements shall be adjusted for changes in valuation by inflating the reported allowable patient-related historical cost of property from the later of July 1, 1976, or the**

date of facility acquisition to the present based on the change in the R. S. Means Construction Index.

(2) The inflation-adjusted historical cost of property per bed as determined above is arrayed to arrive at the average historical cost of property of the median bed.

(3) The average historical cost of property of the median bed as determined above is extended times the number of beds for each facility that are used to provide nursing facility services, to arrive at the fair rental value amount.

(4) The fair rental value amount is extended by a rental rate to arrive at the fair rental allowance.

The rental rate shall be a simple average of the average yield to maturity of the Federal National Mortgage Association Multi-Family rate in effect on the first day of the month that the index is published for each of the twelve (12) months immediately preceding the rate effective date as determined in section 6(a) of this rule. The rental rate shall be updated quarterly on January 1, April 1, July 1, and October 1.

**405 IAC 1-14.6-13 Reporting of financing arrangements; working capital; interest; allocation of loans**

**Authority:** IC 12-8-6-5; IC 12-15-1-10; IC 12-15-21-2

**Affected:** IC 12-13-7-3; IC 12-15

**Sec. 13. (a)** All patient-related property financing arrangements shall be fully and completely disclosed on the forms prescribed by the office.

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(b) Interest costs on borrowed funds used to construct facilities or enlarge existing facilities that are incurred during the period of construction shall be capitalized as part of the cost of the facility or addition.

(c) Interest on working capital loans shall only be recognized if the provider can demonstrate that such loans were reasonable and necessary in providing patient-related services. Working capital interest must be reduced by investment income from any related party. Working capital loans from a related party must be identified and reported separately on the annual financial report. Interest costs on related party working capital loans shall be allowable if they meet all other requirements, the interest does not exceed the rate available in the open market, and such loans are repaid at least annually for a minimum of thirty (30) days. Failure to document the existence of, or adhere to such repayment schedule, shall result in the related party working capital interest costs being disallowed.

(d) Loans covering more than one (1) facility or asset shall apply to the several facilities or assets acquired in proportion to the cost that each item bears to the total cost.

**405 IAC 1-14.6-14 Property; basis; historical cost; mandatory record keeping; valuation**

**Authority:** IC 12-8-6-5; IC 12-15-1-10; IC 12-15-21-2

**Affected:** IC 12-13-7-3; IC 12-15

**Sec. 14. (a)** The basis used in computing the average historical cost of property of the median bed shall be the historical cost of all assets used to deliver patient-related services that meet the following

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**conditions:**

- (1) The assets are in use.**
- (2) The assets are identifiable to patient care.**
- (3) The assets are available for physical inspection.**
- (4) The assets are recorded in provider records.**

**If an asset does not meet all of the requirements prescribed in this section, the cost shall not be included in computing the average historical cost of property of the median bed.**

**(b) The provider shall maintain detailed property schedules to provide a permanent record of all historical costs and balances of facilities and equipment. Summaries of such schedules shall be submitted with each annual financial report, and the complete schedule shall be submitted to the office upon request.**

**(c) Assets used in computing the average historical cost of property of the median bed shall include only items currently used in providing services customarily provided to patients.**

**(d) When an asset is acquired by trading one (1) asset for another, or a betterment or improvement is acquired, the cost of the newly acquired asset, betterment, or improvement shall be added to the appropriate property category. All of the historical cost of the traded asset or replaced betterment or improvement shall be removed from the property category in which it was included.**

**(e) If a single asset or collection of like assets acquired in quantity, including permanent betterment or improvements, has at the time of acquisition an estimated useful life of at least three (3) years and**

a historical cost of at least five hundred dollars (\$500), the cost shall be capitalized and included in the property basis for the approved useful life of the asset. Items that do not qualify under this subsection shall be expensed in the year acquired.

(f) The property basis of donated assets, except for donations between providers or related parties, shall be the fair market value defined as the price a prudent buyer would pay a seller in an arm's-length sale, or, if over two thousand dollars (\$2,000), the appraised value, whichever is lower. An asset is considered donated when the provider acquires the asset without making any payment for it in the form of cash, property, or services. If the provider and the donor are related parties, the net book value of the asset to the donor shall be the basis, not to exceed fair market value. Cash donations shall be treated as revenue items and not as offsets to expense accounts.

**405 IAC 1-14.6-15 Valuation; sale or lease among family members**

Authority: IC 12-8-6-5; IC 12-15-1-10; IC 12-15-21-2

Affected: IC 12-13-7-3; IC 12-15

Sec. 15. (a) If a provider rents, leases, or purchases facilities or equipment from a related party, the historical cost to the related party, not to exceed fair market value, shall be utilized in computing the average historical cost of property of the median bed except as described in this section for the sale of facilities between family members.

(b) If a sale of facilities between family members meets the following conditions, the cost basis of

the facility shall be recognized for the purpose of computing the average historical cost of property of the median bed in accordance with this rule as a bona fide sale arising from an arm's-length transaction, subject to the limitations of subsection (c):

- (1) There is no spousal relationship between parties.
- (2) The following persons are considered family members:
  - (A) Natural parent, child, and sibling.
  - (B) Adopted child and adoptive parent.
  - (C) Stepparent, stepchild, stepsister, and stepbrother.
  - (D) Father-in-law, mother-in-law, sister-in-law, brother-in-law, son-in-law, and daughter-in-law.
  - (E) Grandparent and grandchild.
- (3) The transfer is recognized and reported by all parties as a sale for federal income tax purposes.
- (4) The seller is not associated with the facility in any way after the sale other than as a passive creditor.
- (5) The buyer is actively engaged in the operation of the facility after the sale with earnings from the facility accruing to at least one (1) principal buyer primarily as salaries or self-employment income and not as leases, rents, or other passive income.
- (6) This family sale exception has not been utilized during the previous eight (8) years on this facility.
- (7) None of the entities involved is a publicly held corporation as defined by the Securities and



Exchange Commission.

(8) If any of the entities involved are corporations, they must be family owned corporations, where members of the same family control the corporations through ownership of fifty percent (50%) or more of the voting stock.

(c) In order to establish a historical cost basis in the sale of facilities between family members, the buyer shall obtain a Member Appraiser Institute (MAI) appraisal, which appraisal is subject to the approval of the office. The appraisal shall be done within ninety (90) days of the date of the sale. The historical cost basis for purposes of determining the average historical cost of property of the median bed shall be the lower of the historical cost basis of the buyer or the MAI appraisal of facilities and equipment.

(d) If a lease of facilities between family members under subsection (b)(2) qualifies as a capitalized lease under guidelines established by the American Institute of Certified Public Accountants, the transaction shall be treated as a sale of facilities between family members for purposes of determining the average historical cost of property of the median bed.

405 IAC 1-14.6-16 Unallowable costs; cost adjustments; charity and courtesy allowances; discounts; rebates; refunds of expenses

Authority: IC 12-8-6-5; IC 12-15-1-10; IC 12-15-21-2

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Sec. 16. (a) Charity, courtesy allowances, discounts, refunds, rebates, and other similar items granted by a provider shall not be included in allowable costs. Bad debts incurred by a provider shall not be an allowable cost.

(b) Payments that must be reported on the annual financial report form that are received by a provider, an owner, or other official of a provider in any form from a vendor shall be considered a reduction of the provider's costs for the goods or services from that vendor.

(c) The cost of goods or services sold to nonpatients shall be offset against the total cost of such service to determine the allowable patient-related expenses. If the provider has not determined the cost of such items, the revenue generated from such sales shall be used to offset the total cost of such services.

405 IAC 1-14.6-17 Allowable costs; wages; costs of employment; record keeping; owner or related party compensation

Authority: IC 12-8-6-5; IC 12-15-1-10; IC 12-15-21-2

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Sec. 17. (a) Reasonable compensation of individuals employed by a provider is an allowable cost, provided such employees are engaged in patient care-related functions and that compensation amounts are reasonable and allowable under this section and section 18 of this rule.

(b) The provider shall report on the forms prescribed by the office, all patient-related staff costs